

Contractor's Internal Assessment or Self-Audit of their Property Management System

References:

FAR – Part 45 Government Property

FAR - 52.245-1 -- Government Property

Purpose. The purpose of this document is to provide guidance to property personnel on an approach for evaluation of this requirement within the scope of the Property Management Systems Analysis) (PMSA).

FAR 52-245-1(f)(3) requires contractors to perform self-assessments to evaluate their property management system effectiveness. The clause requires the contractor to disclose significant findings to the Property Administrator (PA). If the self-assessment provides a confidence level of the effective management and/or control of Government property comparable to that afforded by a property management system analysis performed in accordance with DCMA requirements, the PA should integrate the contractor's self-assessment results within the overall audit.

The degree of integration depends on the level of reasonable assurance afforded by the contractor's self-assessment.

Background. A self-assessment process that discovers deficiencies identifies the root causes, and implements effective corrective action is indicative of a healthy property management system.

Prior to the publishing of the revised FAR 52.245-1, many contractors had in place their own property management self-assessment (internal assessments/audits) programs. The FAR clause established the concept as a contractual requirement for all. Accordingly, today, all contractors are contractually required to perform internal assessments and/or audits on their property management system(s) in accordance with FAR 52-245-1(f) (3), and disclose their significant findings to the PA.

These self-assessment requirements are in addition to those audit requirements set forth in Office of Management and Budget Circular A-133 as well as any other statutory requirements; e.g., Sarbanes-Oxley Act of 2002, Securities Exchange Act of 1934. Some contractors have comprehensive internal control programs that integrate these requirements into a corporate approach.

Process. Contractor self-assessments typically fall under two constructs:

1. Formal/structured. Based on:

- Generally Accepted Government Audit Standards
- DCMA's traditional approach (paralleling the audit requirements of the Property Management on Government Contracts Instruction or DoD 4161.2-M, "DoD Manual for the Performance of Contract Property Administration")
- Maturity models—with appropriate process-oriented criteria
- Metrics and statistical process control techniques, or ISO process reviews. Note: ISO audits, internal or external, do not totally fulfill this requirement, as they do not typically address all of the process requirements set forth in the FAR clause, FAR 52.245-1
- International Standards for the Professional Practice of Internal Auditing (Institute of Internal Auditors)
- A combination of the above

2. Informal

- Less structured; less complex
- Walk-throughs
- Interviews/discussions with personnel
- Double checking property records/documentation

Contractor self-assessments may range from simple reviews and/or validations to highly complex audits and assessments, dependent on the complexity of the contractor's property management system. It is recognized that small business concerns typically will not have as sophisticated, detailed and extensive a self-assessment program as major contractors. The PA must use good judgment to ensure that the program provides sufficient oversight without needlessly burdening the contractor.

To the extent possible, depending on the circumstances, contractor self-assessments should provide a level of objectivity as close as possible to that of a PMSA performed by DCMA. Ideally this would be achieved by having the analysis performed by an independent party not associated with the property organization. Sufficient objectivity may be attained by having the assessment performed by property personnel from another location.

In situations where the contractor's operation is relatively small the PA may allow the same people who have custody of the Government property to perform the

audit, subject to review by higher level contractor personnel. If requiring an independent party is not practical or not the optimal way to perform the self-assessment, the PA must document why the method used provides sufficient objectivity to evaluate the effectiveness of the property management system. This is particularly important if the PA intends to integrate the contractor's self-assessment results within the overall audit. In any event the procedures should identify the personnel responsible for performing the self-assessment.

The contractor's audit program as set forth in their property management system should address each of the applicable FAR mandated property management life-cycle processes.

The contractor's written procedures should address the:

- A audit or assessment methodologies to be used; e.g., Generally Accepted Government Auditing Standards, Maturity Models, metrics and statistical process controls, the Instruction's audit protocols.
- Confidence rate and methodology used to compute this rate
- Party responsible for performing the audit
- Frequency of audit
- Processes and outcomes subject to review
- Support documentation and audit evidence
- Requirement for the PA to be notified of significant findings and/or results of such reviews and audits pertaining to Government property
- Reporting requirements and timely distribution of audit and assessment reports
- Corrective action(s) requirements

Many contractors elect to review their own company-owned property during the FAR self-assessment. This is permissible, though not required. Contractor property should not be included in the PA's sampling plan.

Property Administrators' Validation of Contractor's Self-Assessment

The PA shall review the documentation of the internal audit and assessment for compliance with the procedures set forth in the contractor's property management system or other contractual requirements.

If the results of the self-assessment are to be used to evaluate the contractor's risk level or to be integrated into the PMSA, the PA must validate the contractor's internal audit practices through either:

- Visual observations conducted during the contractor's internal audit and/or
- Judgment sampling of the contractor's work papers, verifying the reliability, validity, accuracy and completeness of the data.

It is advisable to walk through the self-assessment with the contractor to gain an understanding of the program, how it works, and what it is expected to achieve. The purpose of this validation will be to confirm that the contractor's self-assessment methodologies and techniques provide the same confidence level (90 percent) used by the Government.

Using the Contractor's Self-Assessment Results in Assessing Risk and/or in Performing PMSAs

The results of the contractor's internal audit should not be the sole basis for evaluating the contractor's property management system. Elements of the contractor's internal audit may be used as a factor in assigning a risk level. Where it has been determined by the PA, through visual observation, judgment sampling, or through the PMSA process, that the contractor's internal audits are reliable, valid, accurate and complete, the PA may reduce the risk assessment level with a commensurate reduction in the frequency of review. Based upon past performance and current internal audit findings, the PA may exempt the certain (compliant) processes from the PA's current year PMSA. In no instance shall review of a process/process segment be exempted any more than the allowable time frame of three years.

The PA may, depending on the circumstances, either integrate the contractor's self-assessment results within the overall audit, or conduct the audit independently. This decision depends largely on the type and scope of contractor operations, level of risk, and degree of confidence in the contractor's property management system. The reliability, validity, accuracy, and completeness of the contractor's self-assessment are factors to consider in deciding whether and how much to integrate its results within the overall audit.

If the contractor's self-assessment methodologies and techniques provide the same confidence level (90 percent) used by the Government the presumption is

that the PA will integrate the contractor's self-assessment results within the overall audit. The PA shall describe the extent of integration of the contractor's self-assessment and the rationale in both the PMSA plan and the PMSA Summary Report.

Some contractors are using the Acceptable Quality Level (AQL) AQL 6.5 end-item inspection quality standard rather than the DoD double sampling plan. This is permissible; use of AQL 6.5 produces results comparable to the DoD double sampling plan. However, PAs should be alert to:

- Process preferences: Some processes are deemed high risk versus low risk– and as such these may require higher AQL's or permit lower AQL's than process capabilities would indicate.
- Class of defects such as major and minor: major defects would generally require lower AQL's than those for minor defects.
- The record of the quality level of previously submitted lots.

Note: If the contractor will be using ASTM 2234, then it is imperative that the contractor define “defect” and the differences between major, minor, and critical defects, as well as what is a defect.

When there are systemic or significant findings disclosed as a result of the contractor's internal audit, the PA should confirm the accuracy of such findings and the sufficiency of the corrective actions. The PA shall not use the information provided by the contractor through the internal audit process as the sole foundation for evaluating the contractor's self-assessment program, especially where the contractor has corrected the deficiencies or has made or is making a good faith effort to correct the deficiencies.

Where the contractor has not made a good faith effort to correct those deficiencies disclosed through the internal audit, or if the corrective actions are insufficient or are not being completed in a timely manner, the contractor's findings shall be incorporated into the PMSA.

Internal Audit and Assessment Records. The PA shall include a copy of the contractor's internal audit or assessment report in the PMSA file.